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NATIONAL SECURITY COUNCIL
WASHINGTON, D.C. 20503

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August 2, 1966

MEMORANDUM FOR THE NATIONAL SECURITY COUNCIL

The enclosed State Department paper on Indonesia will be considered by the National Security Council on Thursday, August 4, 1966.

Bromley Smith
Bromley Smith
Executive Secretary

State Dept. declassification & release instructions on file

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INDONESIA

Background

1. On October 1, 1965, the Indonesian Communist Party joined with elements of the armed forces in an effort to stage a coup by assassination. Six of Indonesia's most prominent generals were killed. Loyal Army elements under General Suharto rallied and crushed the coup attempt within 48 hours. This was the beginning of one of the most dramatic political reversals in recent history. A major nation, which was moving rapidly toward a domestic Communist takeover and was intimately associated with Communist China, within three months destroyed the Communist threat and altered significantly its domestic and foreign orientation.
2. The first element in this political change was the destruction of the Indonesian Communist Party, the fourth largest in the world. The Army hunted down and executed the principal Communist leaders. In the small cities, towns and villages groups of youths, encouraged by the Army and motivated by religion, historic local grievances, and fear of their own fate had the Communists taken power, embarked on a systematic campaign of extermination of Communist Party cadres. While the exact figure will never be known, an estimated 300,000 were killed.
3. The second aspect of this political revolution was a systematic reduction of the powers of President Sukarno with the object of retaining Sukarno as the historic revolutionary figure and symbol of Indonesian unity, but depriving him of the power to govern. This process proceeded in stages. In March, Sukarno was forced to delegate extraordinary powers to Suharto, and Subandrio, Saleh, and others of the coterie of Palace followers who in the past have done Sukarno's bidding were removed from power and imprisoned. This was followed in July by a meeting of the Peoples Consultative Council in which General Suharto's mandate was confirmed and Sukarno was stripped of his position as lifetime President. On July 25 a new cabinet, led by General Suharto and purged of remaining pro-Sukarno figures, was formed. Sukarno remains on the scene, has a capability to obstruct and delay, but has lost the power to initiate or act.
4. Working with General Suharto and the Army were two key leaders: Adam Malik, a former newspaper man whose service as Ambassador to Moscow has modified and rationalized his Marxist orientation; and the Sultan of Djogjakarta - the only public figure with a charismatic appeal to the people of Java comparable to Sukarno's own. In addition, a new and powerful force has emerged on the Indonesian political scene associated with the Army, but apart from it. It is composed of students who have

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come of age in the post-revolutionary period and are fed up with Sukarno, his empty slogans, and the economic chaos and bankruptcy which he has brought on the nation. These students, moving in huge public demonstrations, have been the cutting edge of political change.

5. On the international side there has been a rapid deterioration of Indonesia's relations with Communist China and the Asian Communist states, and a corresponding improvement in Indonesia's relations with the United States and the West. Foreign Minister Malik announced Indonesia's intention to return to the United Nations and its associated international agencies, and Indonesia has already applied to rejoin the International Monetary Fund and the International Bank for Reconstruction and Development. In June, Indonesian and Malaysian delegations met at Bangkok and reached preliminary agreement to bring an end to confrontation, and Malik has indicated an interest in Indonesian participation in Southeast Asian regional organizations.

6. These political developments took place in an economic situation of wild currency inflation, a bankrupt Central Bank, and a foreign debt of \$2.5 billion, whose annual servicing alone comes to more than the country's total annual foreign exchange earnings. The Sultan of Djogjakarta, the minister responsible for economic development, announced early in April a sensible and rational new approach to Indonesia's economic problems. Most of Sukarno's pet projects, which were consuming vast quantities of scarce foreign exchange, have been suspended, and the virtual termination of military confrontation with Malaysia has removed another major resource drain. Money was scraped up earlier this year to purchase rice from Burma and Thailand, and these imports combined with a good domestic rice crop have averted the immediate danger of a food shortage, although without imports, rice may be short in the winter months.

7. There has been, however, only modest progress in dealing with the root causes of Indonesia's economic collapse. The overall cost of living index has increased since October 1, 1965, by a factor of 12 and the amount of money in circulation by a factor of 5. Anti-Chinese riots have intimidated this important entrepreneurial community and caused an exodus of Chinese businessmen and a flight of Chinese capital. The Sultan's sensible words have not been followed by firm measures. The new cabinet inaugurated on July 25 shows considerable strength in the political and social ministries, but the overall level of professional competence of the economic ministers is low and a number of important portfolios remain in the hands of corrupt or incompetent officials. The management capacity of the swollen bureaucracy continues at a low level. It should be noted, however, that Suharto and his associates have up to now given priority attention to the political objectives of establishing themselves in power and restricting the powers of Sukarno. These objectives have been achieved to a major degree. There is no lack of understanding of the severity of Indonesian economic straits and there appears a good prospect that economic matters will now begin to receive more high-level attention.

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United States Interests and Objectives

8. Our traditional interest in Indonesia has been to keep the country out of the hands of its domestic Communists and out of the orbit of Communist China. This objective has, through the events of October 1 and their aftermath, for the time being been achieved. While protecting these major gains, our objective now is to help this populous, potentially rich and strategically placed nation - hitherto a disruptive force in Southeast Asia - overcome the inheritance of Sukarno's mismanagement, develop an effective government, and become a constructive force in the area.

Interests and Objectives of our Allies

9. We share these objectives with many of our friends. The economies of Japan and Indonesia are complementary, and Japan wishes to play a leading role in helping the Indonesian economy get back on its feet. The trading nations of Western Europe are also attracted by Indonesia's natural resources and the potential market of 100 million people. For Australia, New Zealand, Malaysia and the Philippines, an economically healthy, politically friendly Indonesia is essential to their national security. Indonesian recovery is also in the interest of the Soviet Union and its Eastern European allies, who regard Indonesia as a desirable market and source of raw materials. For the USSR as well as for the West, an unaligned Indonesia represents an Asian counterweight to Communist China.

United States Strategy and Past Actions

10. Until late March we kept silent on developments in Indonesia, a policy welcomed by the principal leaders of Indonesia's anti-Communist revolution. However, we gave them private encouragement and demonstrated our support by furnishing small amounts of urgently needed supplies. After the March cabinet reshuffle removed Sukarno's henchmen, we responded to Foreign Minister Malik's request for 50,000 tons of rice under PL-480, Title IV, on near-commercial terms. This was followed in June by a similar sale under Title IV of 75,000 bales of cotton on generous terms of interest and repayment. We have informed Malik that we are prepared to consider a further sale of cotton either direct or for third country processing. We have also encouraged other Free World countries to extend emergency assistance to Indonesia, and Japan, the United Kingdom, Australia and West Germany have made varying amounts of emergency grants and credits available.

11. Our strategy has been to provide, and to encourage other friendly nations to provide, such assistance to Indonesia while its leaders complete the process of political consolidation and place themselves in position to deal with the tough problems of economic reform and reconstruction. We have been working closely with Japan and other countries, who share our objectives in Indonesia, to organize a multilateral approach to Indonesia's longer term problems. This will involve a rescheduling of Indonesia's foreign debt, perhaps preceded by a moratorium, followed by other measures which will help Indonesia deal with inflation and

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restore the shattered export industries on which the economic health of the nation depends. A preliminary meeting of the informal "Aid to Indonesia Club" met in Tokyo on July 19 and a further meeting is planned for mid-September. We and Indonesia's other friends have emphasized that the IMF and the IBRD must play a key role in this reconstruction process. An IMF mission has already visited Indonesia and the new government has issued a formal invitation for the IMF to assist in the development of a stabilization plan.

Future Actions

12. During the short-range period of emergency support we propose to take the following actions:

a. We will continue to use the resources of PL-480 and its successors to provide food and cotton to Indonesia, and may also use CCC credits for this purpose. We are considering sales under PL-480, Title I, to provide rupiahs for our internal needs in Indonesia and to avoid adding to Indonesia's already heavy dollar indebtedness.

b. As soon as we can remove certain legal obstacles to the resumption of aid arising from provisions of the Hickenlooper Amendment (Section 620 (c)) and 620(e) of the Foreign Assistance Act, we intend to request a Presidential Determination, required under Section 620(j) of the same act, that furnishing assistance to Indonesia is in the national interests of the United States. Under a Presidential Determination we propose to provide on Indonesia's request:

- i. civilian participant training in American universities;
- ii. military training in US Service Schools in skills which have a civic action application;
- iii. modest amounts of industrial raw material and spare parts to reactivate US equipment already in use in Indonesia;
- iv. modest amounts of spare parts and technical advisory service to the Indonesian military for the rehabilitation of previously supplied US equipment for use in civic action projects;
- v. text books and reference books at the university level and possibly some technical advice on aspects of an economic stabilization program and other self-help measures; and
- vi. participation, if Indonesia so desires, in regional technical assistance of institutional development programs.

13. Our actions in the longer range economic development effort are difficult to anticipate at this time, since we expect to be working with other countries under the aegis of the IMF and hopefully the IBRD in a

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multilateral setting. As a rough preliminary estimate, based on imperfect data and an uncertain time frame, we might wish to contribute a sum in the range of \$50 million (including PL-480) to a multinational program to provide necessary imports to rehabilitate Indonesia's production plant and to restore badly run-down communications and transportation systems. The amount may vary with the hardness or softness of debt rescheduling terms, since debt relief is a form of aid. Depending on the amount and type of funds needed, it may be necessary to ask Congress for supplementary funds to carry out this long term program. We have been in close touch with key members of Congress on this question, have mentioned this rough estimate of possible future needs, and have found them favorably inclined towards our plans for helping Indonesia. Before any such program is likely to begin, however, Indonesia and its creditors must reach agreement on debt rescheduling and Indonesia must begin to implement a stabilization plan. These in turn will require difficult Indonesian decisions in areas such as budget revenue and expenditure, exchange rates and export incentives. Commitment of our assistance would be related to and paced with Indonesian performance in these areas.

14. At some stage we may wish to consider the return of the Peace Corps. Indonesia will need a broad range of middle-level skills, and when the program is resumed, it should include the widest possible spectrum of Peace Corps activities. Its previous entrance and exit had, however, major political overtones, and until we have clear evidence that the Indonesians want the Peace Corps we mean to proceed with caution.

Anticipated Future Problems

The Army

15. The Indonesian Army now and for some time to come will control the destinies of Indonesia. The Army is a major source of strength, and appears to be solidly united behind Suharto. It has a highly motivated, well trained, professionally competent officer corps. Many officers were trained in the United States, and a number of them have considerable competence in civilian administrative skills. It is an army proud of its record in winning Indonesian independence and determined to protect the fruits of this independence. (It has put down major insurgency movements in virtually every major island of the archipelago.) It is an army that has thus far resisted the temptation of a complete military takeover: it has preferred to work with civilian leaders and maintain its image as the servant rather than the master of the state.

16. The military is also a source of potential weakness and vulnerability. It has consumed over the past six years between 60 and 70% of the Indonesian budget, and may find it difficult to accept a more modest share. It has over 300,000 men under arms and is equipped with sophisticated modern weapons, largely of Russian origin, which it now neither needs nor can afford to maintain. It has a basic distrust of the civilian politicians, little patience with the disorder of free political exchange, and no major commitment to democratic freedoms as we know them. There is a danger that

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the Army may in the course of time move in the pattern of Burma to a military authoritarian state. The armed forces will wish to maintain good relations with the Soviet Union, with whom they have a still unused balance of \$110 million of the original loan for military equipment.

The Indonesian Military and the US

17. As noted above, many Indonesian officers have been trained in US Service Schools. There are, as a consequence, strong US-Indonesian service-to-service ties. We have, therefore, through our attaches in Indonesia and other direct contacts with Indonesian officers, some capability of influencing their policies and actions. This influence carries with it its liabilities. The Indonesian military, and particularly the Army, have been accustomed to turn to us, as well as the USSR, for military supplies. Indonesian officers in informal conversations have indicated an interest in resuming a military assistance program for Indonesia and have spoken of "requirements," running into hundred millions of dollars, which they hope to obtain from the United States. We will have a difficult task of deflecting these completely unrealistic expectations while continuing to maintain our personal ties and influence. In this context, the training and civic action programs proposed in previous paragraphs take on a special importance and urgency.

Unreasonable Request for Aid

18. Indonesia in the past has dealt with its economic problems by skillful use of political and economic leverage to obtain grants and loans from over 30 countries. This habit of looking to others to deal with their economic problems will persist. All preliminary proposals for economic rehabilitation place undue and over-optimistic reliance on a presumed availability of external resources. Indonesia, in short, would prefer to shift the major burden of its economic recovery onto the shoulders of its foreign friends. Malik and the Sultan have indicated their support of the multilateral approach described above, but we must anticipate in the coming months requests for substantial bilateral assistance justified almost exclusively on political grounds. We should attempt to head them off, but if unsuccessful we should not respond favorably without the most careful scrutiny for the following reasons:

a. Favorable response to these large "emergency requests" will reduce domestic pressures and retard rather than accelerate the process of economic reform;

b. Indonesia's capable trading community and its cadre of western-trained, performance-oriented economists who are preaching the need for forceful domestic efforts to cope with the economic situation will be undercut if we respond to emotional political appeals;

c. If we grant further credits we would not only be adding to Indonesia's debt burden, but would also be projecting ourselves into

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political difficulties with them because of the conditions we would have to require to be reasonably certain of repayment.

19. A firm but friendly policy of responding bilaterally to short-range, small-scale emergency needs and confining major assistance to the multi-lateral framework carries acceptable risk for the following reasons:

a. The subsistence sector of the Indonesian economy, embracing 75% of Indonesia's 100 million population, has survived over a decade of monumental mismanagement and continues to have considerable resilience;

b. The fertility of the soil, the general availability of fruit, vegetables and root crops reduces the political pressures of hunger or dire poverty;

c. Indonesia is largely free of absentee landlords and inequitable land distribution;

d. For the time being and for the foreseeable future there is no conceivable political alternative to an Army-dominated government;

e. The political repercussions which they warn us of will operate for the foreseeable future to produce internal reform rather than overthrow of the government.

Indonesia's International Posture

20. While Indonesia has renounced its past close association with Communist China and the Asian Communist powers, we can expect nothing better than non-alignment from Indonesia. Indonesia will continue to remain publicly critical of our actions in Viet-Nam, although Malik from time to time will attempt to soften the impact of these statements by private expressions of understanding. Indonesia, when it returns to the United Nations, will undoubtedly resume its position as one of the more militant of the Asian-African bloc, and while it will no longer stand invariably with Cuba and Albania on major issues in the United Nations, we will continue to find it opposing us on many key questions.

Confrontation

21. The Bangkok Agreement laid the groundwork for termination of confrontation, but it has not yet been ratified by the Indonesian Government. Small-scale border incursions have continued, and there are signs that some elements of the Indonesian Army may attempt to delay ratification in hopes of exacting further concessions from the Malaysians. Malik and Suharto appear sincere in their announced determination to end confrontation, but there may be further delays. In the longer perspective, as Indonesia begins to emerge from its economic difficulties we must anticipate that there will be adventurous elements in Indonesia that may revive efforts to extend control over Malaysia and the Borneo states.

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Timing

22. As we approach the problem of consolidating the gains which the Indonesians themselves have achieved in the past ten months, timing is of paramount importance. We must adjust to the pace which the Indonesians themselves have set for securing their own economic and political salvation. To move too quickly, to show a greater sense of urgency in getting on with the job than the Indonesians themselves feel, will give these resourceful people the idea that they can exact concessions for the privilege of helping them. To move too slowly and to be too rigid in our responses in meeting major needs will encourage a latent threat of complete military takeover, and the emergence of an adventurist totalitarian regime. We are dealing not with an economic infant, but a sick giant with historically proven capacity for quick economic recuperation. We are dealing with a talented and resourceful population, proud, self-confident and determined to stand on its own feet. We are dealing with an island nation where the circumstances of geography and the incredible productivity of its soil tend to break problems into manageable units.

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NSC BRIEFING

INDONESIA

CIA considers the Department of State paper on Indonesia in general a sound and well-argued statement of the problems the US faces in Indonesia.

There are some pertinent developments since the State paper was drafted which should be mentioned:

Since the installation of the cabinet last week, General Suharto apparently has accelerated his efforts to end, formally or informally, the three-year confrontation with Malaysia. Sukarno on 28 July stated in public that the anti-Malaysia campaign should continue. This appears to have provoked General Suharto to the point of forcing Sukarno to give written acknowledgement that confrontation would end.

The other two members of the triumvirate, Foreign Minister Malik and the Sultan of Jogjakarta, hope for a formal end of confrontation by the end of September. Both men are acutely aware that foreign economic assistance may be partly contingent on Indonesia's actual position on confrontation.

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The cabinet is now engaged in filling departmental positions below the ministerial level. The country does not have a very substantial reservoir of managerial competence. An effort is apparently being made, however, to bring in technically qualified personnel, particularly in economic and financial departments and in those ministries where concessions to Sukarno resulted in the appointment of unqualified ministers.

Our greatest concerns continue to be Indonesia's economic problems, and the speed with which the new cabinet can come to grips with these problems.

In this connection, I feel I must note two basic CIA reservations with the position paper. One is our belief that for some time to come we should be thinking in terms of a salvage operation; it is too optimistic to talk in terms of stabilization and recovery, given the magnitude of the problem.

The other is that we are not very sanguine about concerted multilateral action to cope with the Indonesian situation. We think other creditor nations, particularly the Europeans, will tend to move slowly, go it alone, and take a fairly hard line toward Indonesia.

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